BEFORE THE

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION, **Complainant,** **v.** **PUGET SOUND ENERGY,** **Respondent.**	**DOCKET UG-230968**

INITIAL POST-HEARING BRIEF OF PUGET SOUND ENERGY

NOVEMBER 7, 2024

PUGET SOUND ENERGY

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I. INTRODUCTION

1. On November 22, 2023, Puget Sound Energy ("PSE" or "the Company") filed with the Washington Utilities and Transportation Commission ("WUTC" or "Commission") revised tariff sheets for its natural gas Schedule 111, Greenhouse Gas Emission Cap and Invest Adjustment, with rates reflecting the Company's forecasted Climate Commitment Act costs and revenues for 2024. PSE's Schedule 111 is an existing pass-through tariff with tracking and true-up functions that addresses PSE's Climate Commitment Act costs and revenues. PSE's filing requested authorization to fund decarbonization projects by setting aside $23 million of the Company's projected no cost allowances revenues. PSE filed a substitute Schedule 111 on December 19, 2023, amending its proposal to spread the withholding of the proceeds for targeted electrification projects over the three years of 2024 to 2026, setting aside $7.7 million in estimated proceeds for no cost allowances during the 2024 rate period.

2. PSE's revised tariff sheets were discussed at the Commission's December 21, 2023, open meeting, in which Commission staff ("Staff") recommended that the Commission suspend the matter and initiate an adjudication. On December 22, 2023, the Commission issued Order 01 in Docket UG-230968 suspending the tariff sheets filed by PSE on November 22, 2023, as revised on December 19, 2023, but allowing the proposed rates to become effective on January 1, 2024, on an interim basis, subject to refund, pending the Commission's final determination in this Docket.

3. This opening brief presents PSE's position that the Commission should decline to impose a risk-sharing mechanism in this proceeding. As discussed below, a risk-sharing mechanism conflicts with the legislative intent and operation of the Climate Commitment Act Cap and Invest Program, increases risks and costs, and inserts a strict and permanent mechanism into a nascent program that has not been given a chance to perform as intended.

II. BACKGROUND FACTS

4. On May 17, 2021, Governor Jay Inslee signed into law Engrossed Substitute Senate Bill 5126, more commonly referred to as the Climate Commitment Act.[1] The Climate Commitment Act establishes a comprehensive, market-based program intended to reduce state greenhouse gas emissions to meet the state's reduction goals in RCW 70A.45.020, which the legislature updated in 2020. The Climate Commitment Act started on January 1, 2023, and the Department of Ecology held the first emissions allowance auction on February 28, 2023. PSE is a covered entity, as defined in RCW 70A.65.080, and must participate in the compliance program by acquiring compliance instruments (allowances or offsets) for both its electric and natural gas local distribution company ("LDC") operations.[2]

5. The Climate Commitment Act is an economy-wide, market-based system designed to reduce overall greenhouse emissions within Washington.[3] The Climate Commitment Act covers many sectors of the economy and not a single aspect (e.g., electric or natural gas LDC utilities). The Climate Commitment Act does not require any single entity to reduce greenhouse gas emissions.[4] Rather, the Climate Commitment Act requires covered entities to acquire compliance instruments (allowances or offset credits) to cover greenhouse gas emissions over a four-year compliance period.[5] As the total number of available allowances declines, each covered entity can make a choice—the covered entity must reduce emissions or acquire compliance instruments to cover emissions obligations, whichever is more cost-effective.

6. Washington's Cap-and-Invest Program was modelled on California's cap-and-trade program. Indeed, one intent of the design of the Cap-and-Invest Program was for it to be sufficiently similar to the California cap-and-trade program to allow linkage of the programs.

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[1] Engrossed Substitute Senate Bill 5126, codified as Chapter 70A.65 of the Revised Code of Washington (RCW), available at https://lawfilesext.leg.wa.gov/biennium/2021-22/Pdf/Bills/Session%20Laws/Senate/5126-S2.SL.pdf?q=20240408121924.
[2] *See* Steuerwalt, Exh. MS-1T at 2:9-13.
[3] RCW 70A.65.005.
[4] *See* Steuerwalt, Exh. MS-1T at 4:6-9.
[5] *See* Steuerwalt, Exh. MS-1T at 4:9-11.

Specifically, the natural gas provisions of Washington's cap-and-invest program were intentionally designed to match those in the California cap-and-trade program.[6]

7. Nothing in the Climate Commitment Act authorizes a risk-sharing mechanism, and nothing in the Climate Commitment Act requires natural gas LDCs like PSE to reduce emissions of their customers. Instead, the Climate Commitment Act requires natural gas utilities to acquire a volume of compliance instruments (allowances or offset credits) sufficient to cover the emissions from the combustion of natural gas delivered to customers.[7] The intent of the Climate Commitment Act is to achieve emissions reductions in the most cost effective manner across the economy and does not require specific emissions reductions by any entity, even covered entities, like PSE, subject to compliance under the Climate Commitment Act.[8] The Climate Commitment Act is intended to send a price signal to encourage decarbonization by people and facilities that have emissions.[9] That price signal would get passed through to customers so customers will have incentive to conserve or decarbonize, and PSE will have the obligation to comply with the statute to help customers along that decarbonization route.[10] So long as PSE satisfies its compliance obligations under the Climate Commitment Act by either reducing emissions or acquiring compliance instruments, the Commission should be satisfied that the law is producing its intended results.[11]

8. The Commission ordered PSE to submit a risk-sharing mechanism proposal pursuant to Order 01 in Docket UG-230470. The Commission's Order 01 in that docket, however, expressed no clear intent to implement any risk-sharing mechanism. Rather, the Commission initiated this adjudication to consider a potential risk-sharing mechanism in the context of determining whether PSE's revisions to Schedule 111 are fair, just, reasonable, equitable, and sufficient.[12]

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[6] *See* Steuerwalt, Exh. MS-1T at 4:17-5:2.
[7] *See* Steuerwalt, Exh. MS-1T at 5:15-19.
[8] *See* RCW 70A.65.005.
[9] *See* Kuzma, Tr. 95:2-8.
[10] *See* Kuzma, Tr. 95:2-8.
[11] *See* Steuerwalt, Exh. MS-1T at 6:18-21.
[12] *See* Docket UG-230968, Order 01 ("Order 01") at ¶ 15.

The Commission is certainly not required to implement a risk-sharing mechanism, and this proceeding was initiated to explore not only PSE's proposal for a risk-sharing mechanism, but to determine whether a risk-sharing mechanism is needed at all to establish fair, just, reasonable, equitable, and sufficient rates. "The issue of a risk-sharing mechanism for CCA compliance costs is a complex one, and the Commission would benefit from a full record, including testimony and briefing from the parties."[13]

9. Most of the parties in this proceeding now agree for various reasons that a risk-sharing mechanism is not appropriate now. The legislative intent behind the Climate Commitment Act was to create a market-based program to reduce emissions, and distorting market price signals to end-use customers and creating implementation complexities through a risk-sharing mechanism is not useful or warranted at this time. Staff ultimately prefers no risk-sharing mechanism and instead requests that the Commission eliminate Schedule 111 altogether and require PSE to recover all Climate Commitment Act costs in base rates.[14] Staff's risk-sharing mechanism is presented only as an alternative to its preferred proposal.[15] The Alliance of Western Energy Consumers's ("AWEC") comments reflect opposition to a risk-sharing mechanism at this time and concerns about a risk-sharing mechanism overall.[16] Public Counsel is opposed to Staff's preference for putting Climate Commitment Act costs into base rates[17] and submits that the Commission should reject all the proposals presented in this proceeding.[18,19] At this point, only

[13] *Id.* at ¶ 14.
[14] *See* McGuire, Exh. CRM-1T at 31:21-32:4.
[15] "Does Staff have an alternative recommendation in the event the Commission declines to order PSE to eliminate Schedule 111 and move CCA compliance costs into base rates?" "A. Yes. If the Commission declines to adopt Staff's recommendation to order PSE to eliminate the CCA tracker, the Commission should nevertheless order PSE to establish a RSM effective January 1, 2025." McGuire, Exh. CRM-1T at 33:11-16.
[16] *See* AWEC Comments in Docket U-230161 at note 7, ¶ 2 (Nov. 3, 2023). *See also* AWEC Comments in Docket UG-230968 (Dec. 19, 2023).
[17] *See* Earle, Exh. RLE-1CT at 27:13-15.
[18] *See* Earle, Exh. RLE-1CT at 27:1-2 and Earle, Tr. 138:1-140:3. *See also* Earle, Tr. 142:14-144:18.
[19] Further, Public Counsel believes if the Commission ultimately decides to implement a risk-sharing mechanism, it should do so after this first Climate Commitment Act compliance period concludes in 2026 and after modeling improves. *Id.*

JEA[20] supports implementing a risk-sharing mechanism. Not only is such mechanism not required by the Climate Commitment Act,[21] but the mechanism JEA proposes to utilize cannot be implemented.

III. LEGAL STANDARD

10. The ultimate legal question in tariff filing is whether the rates and charges proposed by a utility are in the public interest and are fair, just, reasonable, and sufficient.[22] In making these determinations, the Commission is bound by the statutory and constitutional mandate that a regulated utility is entitled to (i) reasonable and sufficient compensation for the service it provides,[23] and (ii) the opportunity to earn "a rate of return sufficient to maintain its financial integrity, attract capital on reasonable terms, and receive a return comparable to other enterprises of corresponding risk."[24]

IV. THE COMMISSION SHOULD DECLINE TO IMPOSE A CLIMATE COMMITMENT ACT RISK-SHARING MECHANISM

A. A Risk-sharing Mechanism is a Complex Issue, and Most Parties Agree that the Commission Should Decline to Impose One at This Time

11. Most of the parties in this proceeding agree that a Climate Commitment Act risk-sharing mechanism is not appropriate at this time. Other than that consensus, however, there is virtually no alignment among any parties over the most basic questions regarding PSE's Climate Commitment Act cost recovery, and the Commission should avoid adding complications to that process by imposing a risk-sharing mechanism. Rather than providing clarity and answering questions regarding how to best recover Climate Commitment Act compliance costs, the

[20]Climate Solutions, NW Energy Coalition, and Washington Conservation Action make up the collective party Joint Environmental Advocates ("JEA").
[21]Namely, that each covered entity must reduce its own emissions, rather than avail themselves of the market created by the Climate Commitment Act.
[22] RCW 80.28.020; *People's Org. for Wash. Energy Res. v. WUTC*, 104 Wn.2d 798, 808 (1985) (*en banc*) ("*POWER*"); *see also* RCW 80.28.425(1) (the Commission can also consider equitable factors to the extent such factors affect the rates, services, and practices of a gas or electrical company regulated by the Commission).
[23]*POWER*, 104 Wn.2d at 808; *Puget Sound Traction Light & Power Co. v. Pub. Serv. Comm'n*, 100 Wn. 329, 334 (1918) (*en banc*); RCW 80.28.010(1).
[24]*WUTC v. Avista Corp*., Dockets UE-991606, et al., Third Supp. Order ¶ 324 (Sept. 29, 2000).

evidence and opinions presented in this proceeding have only raised additional questions and highlighted contested positions on even the most basic and fundamental ratemaking issues.[25]

1. Staff requests elimination of PSE's Climate Commitment Act tracker, altogether

12. Staff initially supported PSE's proposal to recover costs of allowance purchases and proceeds through PSE's Climate Commitment Act tracker, Schedule 111.[26] Regarding revisions to the Climate Commitment Act tracker, which initiated this proceeding, Staff requested only that PSE amend its revisions to spread the withholding for decarbonization projects over three years.[27] PSE did so.[28] Now, however, Staff completely changes its position, goes back on its support for Schedule 111, and recommends instead that the Commission eliminate the Climate Commitment Act tracker altogether. Staff argues now that the Commission should include all Climate Commitment Act compliance costs in PSE's base rate revenue requirement calculations.[29]

13. No party agrees with JEA that a risk-sharing mechanism is appropriate, and there is not even a consensus on the fundamental purpose behind a risk-sharing mechanism. Some parties think a risk-sharing mechanism is supposed to share risks, and others think it is supposed to reduce emissions. Specifically, Staff and PSE believe that a risk-sharing mechanism is meant to share the financial risk of acquiring compliance instruments that vary in price with every auction.[30] However, JEA argues that a risk-sharing mechanism should force PSE to respond to

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[25] *See, e.g.,* Earle, Exh. RLE-1CT at 14:6-16, disagreeing with Staff's method for evaluation for whether a tracker is in the public interest.

[26] Docket UG-230968, Staff Open Meeting Memorandum, Dec. 21, 2023 ("Staff Memo").

[27] Staff Memo at p. 3 ("Staff has reviewed PSE's proposed Schedule 111 rates and supporting work papers and, with the exception of the issue discussed immediately above, finds the rates to reasonably reflect PSE's costs of allowance purchases and proceeds from the sale of allowances in calendar year 2024. If PSE is willing to submit replacement tariff pages reflecting a credit rate that spreads the $23 million for decarbonization projects over three years (2024 through 2026), Staff believes that the resulting rates would be fair, just, reasonable, and sufficient.") (Dec. 21, 2023).

[28] *See* Order 01 at ¶ 6.

[29] *See* McGuire, Exh. CRM-1T at 3:7-10.

[30] *See* McConnell, Exh. KM-1T at 3:3-4:19. *Also,* "As a threshold matter, Staff agrees with the Company that the design of the RSM should be focused on allowance instrument market financial risks rather than total emission variance risk." McConnell, Exh. KM-1T at 4:5-7.

the price signal for Climate Commitment Act compliance by reducing customer emissions, even if those reductions are not cost-effective and would result in higher costs for consumers.[31] As explained below, JEA's interpretation of the Climate Commitment Act is flawed and its risk-sharing mechanism has no support in the language or intent of the Climate Commitment Act.

2. AWEC shares PSE's concerns, and states that a risk-sharing mechanism should not be adopted in this proceeding

14. Although AWEC is a party to this adjudication,[32] it declined to submit testimony in this docket but submitted comments opposing a risk-sharing mechanism, both in this proceeding and in Docket U-230161. For example,

> AWEC continues to have serious concerns about the development of a risk sharing mechanism, at least at this time. As AWEC noted in its September 7th comments, the Cap-and-Invest program is, by design, a market-based mechanism, meaning that the market is intended to provide the incentive to reduce emissions. The program also includes noncompliance penalties, which further serve to incentivize compliant utility actions. Accordingly, to the extent a risk-sharing mechanism is designed to reduce emissions beyond what will occur naturally through the Cap-and-Invest program and in a manner that increases costs to customers, AWEC is firmly opposed to such a mechanism.[33]

15. More recently, AWEC's comments in this proceeding expressed its lingering opposition to a risk-sharing mechanism. "If the Commission remains inclined to adopt a CCA Risk-Sharing Mechanism, it should do so after issuing guidance on both substance and process in Docket U-230161."[34]

3. Public Counsel opposes all proposals, arguing the timing is wrong to impose a risk-sharing mechanism

16. Public Counsel filed no testimony in response to PSE's risk-sharing mechanism, preferring instead to wait until cross answering testimony before opposing all the proposals presented in this proceeding.[35] Rather than impose any risk-sharing mechanism now, and rather

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[31] *See* McCloy, Exh. LM-1T at 9:14-14:7.
[32] *See* Order 02, Prehearing Conference Order, at ¶ 6 (Feb. 12, 2024).
[33] Steuerwalt, Exh. MS-1T at 9:17-10:4, *citing* AWEC Comments in Docket U-230161 at note 7, ¶ 2 (Nov. 3, 2023).
[34] Docket UG-230968, Comments of AWEC (Dec. 19, 2023).
[35] *See* Earle, Exh. RLE-1CT at 2:1-12.

than eliminate PSE's Climate Commitment Act tracker, Public Counsel recommends that Staff and PSE simply wait, then try again.[36] Public Counsel testifies that there is too much uncertainty over the future of the Climate Commitment Act and not enough data with which to measure PSE's market performance.[37]

17. Public Counsel not only opposes Staff's risk-sharing mechanism, it opposes Staff's primary proposal to imbed all Climate Commitment Act costs in base rates. Dr. Earle testifies that the timing of the Climate Commitment Act compliance periods and the timing of multi-year rate cases necessitate too much uncertainty that would result in higher costs for all customers:

> Because the opportunity to buy and sell allowances to cover a utility's obligations extend through the four-year compliance period plus 10 months, allowance cost forecasts for a GRC period must consider the demand over the four-year compliance period, and prices over the whole four-year compliance period plus the additional 10-month true-up period. A GRC period that includes a 10-month true-up period must include forecasts for both the current compliance period as well as the next. For example, if PSE's next GRC for the years 2027 and 2028, is filed in 2026, under Staff's proposal, PSE would have to sometime in late 2025 forecast prices and demand levels for 2026 through October 31, 2031. It would also have to use these forecasts to determine its strategy for through October 31, 2031, to forecast its costs.[38]

With so many uncertain factors, Public Counsel explains, Staff's proposal to eliminate Schedule 111 would unnecessarily increase risks for both customers and the Company.[39] PSE agrees.

18. PSE witness Jason Kuzma presented multiple hypotheticals that demonstrate the fluctuations that would likely occur if the Commission grants Staff's primary proposal and eliminates Schedule 111 to move all Climate Commitment Act costs to be recovered in base rates.[40]

> These hypotheticals demonstrate that the inclusion of CCA compliance costs in the PSE base rate revenue requirement for natural gas operations would result insignificant over- and under-

[36] *See* Earle, Exh. RLE-1CT at 24:19-25:2.
[37] *See* Earle, Tr: 144:16-20.
[38] Earle, Exh. RLE-1CT at 10:5-22. *Also,* Earle, Tr. 144:16-20.
[39] *See* Earle, Exh. RLE-1CT at 10:21-22.
[40] *See* Kuzma, Exh. JK-3T at 69:1-79:12.

> recoveries due to circumstances outside the control of PSE and the Commission. Small changes in large numbers have large results.[41]

After Jason Kuzma demonstrated the likely outcome of pushing Climate Commitment Act costs into base rates, PSE witnesses Jamie Martin and Todd Shipman provided real world implications of what those fluctuations would mean to the larger market, PSE's ability to purchaser debt, and PSE's financial integrity.[42]

19. As PSE's Senior Vice President and Chief Financial Officer, Jamie Martin, explains, Staff's proposal is based on a fundamental misunderstanding of bedrock principles related to risks and returns in regulatory law.[43] Investors have a finite amount capital, and they are more likely to make investments in a utility if they can expect returns commensurate with comparable investment options with corresponding risks.[44] If the Commission were to adopt Staff's proposal and require a risk-sharing mechanism for all adjustment mechanisms implemented by PSE and approved by the Commission over the decades, then PSE's cash flows, earnings, and returns on equity would become more volatile relative to peer utilities across the Country.[45] Adoption of this proposal could create a serious and potentially material disconnect when the Commission considers cost of capital studies and peer group analyses when establishing returns on equity for PSE in future general rate proceedings.[46]

B. A Risk-sharing Mechanism Raises Multiple Legislative and Legal Concerns

1. Adding a risk-sharing mechanism fundamentally changes the program from the one passed by legislators

20. The diverging opinions over fundamental Climate Commitment Act cost recovery issues highlight the concerns PSE has raised in this proceeding about imposing a risk-sharing mechanism when there is no legislative or policy intention or direction to do so. Nothing in the

[41] Kuzma, Exh. JK-3T at 80:1-11.
[42] *See* Martin, Exh. JLM-1Tr and Shipman, Exh. TAS-1T.
[43] *See* Martin, Exh. JLM-1Tr at 4:7-11.
[44] *See* Martin, Exh. JLM-1Tr at 4:8-5:16, citing landmark cases *Bluefield* (*Bluefield Water Works Improvement Co. v. Pub. Serv. Comm*., 262 U.S. 679 (1923) and *Hope* (*Fed. Power Comm'n v. Hope Natural Gas Co*., 320 U.S. 591 (1944)).
[45] *See* Martin, Exh. JLM-1Tr at 8:15-9:1.
[46] *See* Martin, Exh. JLM-1Tr at 8:15-9:1-4.

Climate Commitment Act requires or authorizes the Commission to implement a risk-sharing mechanism and, although the Commission has broad ratemaking authority, a risk-sharing mechanism is not appropriate in this context.

21. PSE witness Matt Steuerwalt played a key role in the design and passage of the Climate Commitment Act, and no witness in this proceeding has more insight into the considerations deliberated by the legislature in passing the Climate Commitment Act. As Steuerwalt testified, the intent of the Climate Commitment Act is to achieve emissions reductions in the most cost effective manner across the economy. It requires natural gas utilities like PSE to acquire a volume of compliance instruments at market sufficient to cover the emissions from the combustion of natural gas delivered to customers. As the total number of available allowances declines, PSE can make a choice—reduce emissions or acquire compliance instruments to cover emissions obligations, whichever is more cost-effective.[47] The Climate Commitment Act does not require specific emissions reductions by the utility or any customer at any cost. So long as PSE satisfies its compliance obligations under the Climate Commitment Act by either reducing emissions or acquiring compliance instruments, the law is working as it should. Inserting a risk-sharing mechanism into a program that did not contemplate one necessarily interferes with the way the legislators intended the program to work.

22. As Matt Steuerwalt testified at hearing, if the policy makers had intended for covered entities to participate in risk and cost sharing with customers, the remainder of the bill would have likely looked different.[48] To add a mechanism into a program that did not account for one is to change the program altogether. The Climate Commitment Act is a carefully crafted piece of legislation that allows covered entities various ways to decarbonize, but it involves assumptions that PSE and other utilities would fulfill its legislative duty to serve.

> I don't think policy makers contemplated a universe in which the question of whether we were supposed to continue to serve customers was at issue. I think people thought you are going to

[47] *See* Steuerwalt, Exh. MS-1T at 5-14.
[48] *See* Steuerwalt, Tr. 91:8-11.

> keep serving customers. We are going to impose this compliance obligation on you as a way of not imposing a compliance obligation on 900,000 individual customers, right, and you are going to have to serve them with whatever resource they demand.[49]

23. The Climate Commitment Act placed the compliance obligation on covered entities, not customers, and the law intends the market itself to communicate to customers how they should decarbonize. In PSE's case, that signal is communicated through its Schedule 111 tariff. If the costs of Climate Commitment Act compliance are shared through the use of a risk-sharing mechanism, then the price of carbon is muted for the customer, and they will not hear the message as intended.

24. Imposing a risk-sharing mechanism also prematurely inserts unnecessary complications into a process that has not even yet completed one compliance period. On this, Public Counsel,[50] Staff,[51] and PSE[52] can agree. At this early stage of Climate Commitment Act implementation, it is not possible to design an equitable, fair, and reasonable risk-sharing mechanism. Staff acknowledges that there is insufficient detailed analysis at this early stage of Climate Commitment Act compliance, but it mistakenly raises this concern as a reason to eliminate Schedule 111 beyond the Climate Commitment Act's first compliance period.[53] Public Counsel urges the Commission to allow PSE and Staff to discuss and agree on a risk-sharing mechanism to be presented in PSE's next multi-year rate plan for the next Climate Commitment Act compliance period, beginning in 2027.[54] Regardless of whether it is premature to initiate a risk-sharing mechanism or to operate Schedule 111 "in perpetuity," the reasoning is apt and undisputed. The Commission should allow PSE time to operate the Climate Commitment Act tracker as it was intended for at least one Climate Commitment Act period before changing it.

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[49] Steuerwalt, Tr. 92:4-12.
[50] *See* Earle, Tr. 138:1-139:9.
[51] *See* McGuire, Exh. CRM-1T at 4:1-2.
[52] *See* Steuerwalt, Exh. MS-1T at 15:3-16:5.
[53] *See* McGuire, Exh. CRM-1T at 4:1-2.
[54] *See* Earle, Tr. 138:23-139:9.

25. As Steuerwalt explained, risks already surround Climate Commitment Act compliance without introducing additional uncertainty of a risk-sharing mechanism, such as (i) the shifting policy landscape with aspects of rulemaking still underway or future rulemaking expected, (ii) price and availability of future emissions reduction technologies, and (iii) linkage of Washington's Cap-and-Invest Program with similar market-based mechanisms in other jurisdictions.[55]

26. Additionally, the Commission recently recognized the complexity associated with the development of performance-based measures due to the layering of legislative requirements:

> Additional complexity exists in Washington state for developing a [performance-based rates] framework with the layering of legislative requirements (e.g., [multiyear rate plans], the Clean Energy Transformation Act (CETA) of 2019, decarbonization requirements under the Climate Commitment Act (CCA) of 2021; and the Washington Decarbonization Act for Large Combination Utilities of 2024 (ESHB 1589), and other factors such as: increased frequency and severity of extreme weather events, geopolitical issues, greater focus of equity and energy justice, and development of regional electricity markets. Innovation is required to meet these requirements, expectations, and developments.[56]

27. The legal landscape surrounding the Climate Commitment Act remains in flux, and imposing new obligations on the Climate Commitment Act framework now will reduce PSE's ability to decarbonize. PSE is obligated to provide as much natural gas as demanded by its customers, but State laws and policies simultaneously limit the ability of gas companies to transition to new fuels. For example, RCW 80.28.385 permits natural gas companies to supply renewable natural gas for a portion of the natural gas sold or delivered to their retail customers but limits the cost of volume of renewable natural gas by imposing a cap of "five percent of the

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[55]Steuerwalt, Exh. MS-1T at 15:4-11.

[56]Steuerwalt, Exh. MS-1T at 16:2, citing *In the Matter of the Proceeding to Develop a Policy Statement Addressing Alternatives to Traditional Cost of Service Rate Making, Interim Policy Statement Addressing Performance Measures and Goals, Targets, Performance Incentives, and Penalty Mechanisms*, Docket U-210590 (Apr. 12, 2024) ("Interim Policy Statement"), note 3, at ¶ 17. The Commission also noted in the Interim Policy Statement that "[performance incentive mechanisms] are not always the best incentive for utility action as there may be other motivators such as legal liability or reputational risk that provide adequate intrinsic motivation not advanced by an additional financial reward or penalty." *Id*. at ¶ 19.

amount charged to retail customers for natural gas."[57] PSE is currently approaching the five percent cap.[58] This restriction severely limits the ability of natural gas companies to rely on renewable natural gas to decarbonize customer fuel supply, a limitation compounded by the fact that renewable natural gas sells at a premium price when compared to traditional natural gas.[59]

2. A risk-sharing mechanism will contradict long-standing regulatory principles.

28. A risk-sharing mechanism changes the operation and intent behind the Climate Commitment Act and potentially interferes with the Commission's other long-standing regulatory tools. An important and long-standing regulatory principle involves the recovery of prudent costs: utilities should be able to recover prudently-incurred operation costs necessary to meet customer loads.[60]

29. Parties at the evidentiary hearing appear under the assumption that a tracker inevitably passes through all Climate Commitment Act costs to customers automatically, with no scrutiny or ability to reject imprudent costs.[61] This, of course, is not true and ignores a critical tool in the Commission's regulatory framework. PSE carries the burden to demonstrate that any and all Climate Commitment Act costs passed through in Schedule 111 must be prudently incurred.[62] As AWEC pointed out in its December comments, even though the source of funds for decarbonization projects is from auction proceeds (and even if they are passed through in a tracker), PSE maintains the obligation of providing evidence that allows the Commission to evaluate the prudence and reasonableness of costs and revenues reflected in rates.[63] "And the

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[57] RCW 80.28.385(1).
[58] *See* Steuerwalt, Exh. MS-1T at 13:11.
[59] *See* Steuerwalt, Exh. MS-1T at 13:11-13.
[60] *WUTC* v. *Avista Corp., d/b/a Avista Utils.,* Dockets UE-050482 and UG-050483 (*consolidated*), Order 05 at ¶ 22 (December 21, 2005).
[61] *See, e.g.,* exchange between counsel for Staff and PSE witness Matt Steuerwalt regarding recovering "every cost that the company incurs in order to serve customers:" Callaghan and Steuerwalt, Tr. at 77:8-22. *See also,* exchange between counsel for Public Counsel and Matt Steuerwalt: "Q: We should just trust you to get it right?" "A: No, I'm not saying that at all, sir. I'm saying we have -- the Commission has the regulatory authority using its existing mechanisms to examine whether we are making cost effective choices to comply with CCA for customers." O'Neill and Steuerwalt, Tr. at 88:7-12.
[62] Kuzma, Exh. JK-3T 89:3-6.
[63] *See* AWEC comments at ¶ 4, Dec. 19, 2023.

Commission must still ensure that rates are fair, just, reasonable and sufficient."[64] This means that PSE must show that the decision to purchase Climate Commitment Act compliance instruments is a decision that a reasonable board of directors and company management would have made given what they knew or reasonably should have known to be true at the time they made the decision.[65]

V. IF THE COMMISSION IMPOSES A RISK-SHARING MECHANISM AT THIS TIME, PSE'S IS THE MOST SENSIBLE OF THE THREE PROPOSALS PRESENTED

30. Only Staff, PSE, and JEA submitted risk-sharing mechanism proposals in this proceeding, and no two parties agree on any proposal. PSE's proposal is a simple mechanism designed to balance cost recovery with maintaining the Company's financial viability. It includes a single-side risk-sharing mechanism, where PSE shares risk only if costs exceed expectations and the Company is in a financially viable situation, while all resulting benefits are passed on to the customers.[66] This financial viability is measured through a financial earnings test, which ensures cost-sharing mechanisms reflect both market dynamics and the financial stability of PSE. The mechanism reflects the most recent policy guidance issued by the Commission on performance incentive mechanisms in Docket U-210590.[67] It is based on fundamental principles of cost recovery mechanisms, such as addressing factors reasonably within the control of the utility:

> **6. Reasonably within the utility's control:** Metrics will seek to measure factors that are reasonably affected by the utility's actions and not be entirely based on external influences (i.e., market prices, weather, and mean area median incomes) without limiting

[64] *Id.*

[65] *See WUTC v. Puget Sound Energy*, Docket UE-031725, Order 12 at ¶ 19 (Apr. 7, 2004). Public Counsel witness Dr. Robert Earle reminds the Commission and parties that market forecasts and other system details that may instruct such decisions are evolving and will benefit with additional time and experience. Earle, Exh. RLE-1CT at 25:1-27:2.

[66] *See* Mickelson, Exh. CTM-4T at 2:17-21.

[67] *See, e.g.,* Interim Policy Statement.

> the Commission's authority and to the extent they do not hinder the advancement of equity and energy justice.[68]

PSE's proposal is supported by thorough statistical analysis,[69] and PSE undertook and produced comprehensive reporting to demonstrate and ensure that the variables contained in Schedule 111 are reliable.[70]

A. Staff's Proposal is Generally Acceptable, But its Earnings Test Should Be Rejected in Favor Of PSE's

31. Staff's proposal introduces caps as an alternative approach to PSE's earnings test, but the caps are drastic, arbitrary, and not well thought out. Accordingly, PSE recommends that Staff's earnings test be replaced with PSE's well-supported earnings test.

32. Staff's response testimony suggests a 10-basis points cap placed upon the Company's annual return on equity, but Staff does not clarify what the 10-basis point cap is applied to (e.g., rate base, net operating income, etc.) or even which party the cap impacts (*i.e.,* PSE or the customer) if a compliance amount is above such cap.[71] PSE issued several data requests to Staff in attempt to understand how Staff would implement the mechanism. Specifically, PSE requested that Staff provide a working model of its risk-sharing mechanism and describe in detail the calculation and application of Staff's proposal.[72] Staff's response was simply that it had no such description and did not have a working model.[73] At the evidentiary hearing, Staff suggested that if PSE had lingering questions about Staff's proposal, the Company could simply request clarification from the Commission following its order approving it.[74] Staff's presumptive suggestion attempts to shift the burden to PSE and, apparently, the Commission to figure out Staff's proposal without any workpapers, analysis, or other evidentiary support. As PSE witness

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[68] *See* Steuerwalt, Exh. MS-1T at 8:13-19, citing Climate Commitment Act Workshop Series, slide 12, Docket U-230161 (Nov. 8, 2023), available at https://apiproxy.utc.wa.gov/cases/GetDocument?docID=139&year=2023&docketNumber=230161.

[69] *See* Mickelson, Exh. CTM-1CT at 4:5-12:14.

[70] *See* Kuzma, Exh. JK-4T at 10:1-68:15.

[71] *See* Mickelson, Exh. CTM-4T at 4:5-12.

[72] *See* Exh. CTM-5.

[73] Exh. CTM-5.

[74] *See* Callaghan, Tr. 111:16-112:9.

Chris Mickelson pointed out at the hearing, it is the responsibility of the proposing party to provide a clear, precise proposal so people can understand what they analyze.[75]

33. It is important to remember, however, that Staff and PSE prefer no risk-sharing mechanism at all, and their mechanisms are only an alternative to their primary proposals. While no parties agree on a mechanism, Staff, Public Counsel, and PSE all oppose JEA's proposal.

B. JEA's Risk-Sharing Mechanism is Extreme and Would Harm PSE

1. JEA's risk-sharing mechanism is arbitrary, extreme, and increases risks

34. PSE's proposal is a financial risk mechanism based on Climate Commitment Act compliance instruments,[76] and it is supported with sound statistical analysis using backward looking, actual market analysis rather than the uncertain forward market.[77] As explained below, Public Counsel warns against using forward markets as the basis for a risk-sharing mechanism.

35. JEA's proposal is riskier and costlier because it is focused on emissions reductions rather than compliance instruments. JEA's mechanism includes a rigid cap and strict earnings test and, as discussed above, begins with the incorrect interpretation that covered entities like PSE must comply with the Climate Commitment Act "primarily through emissions reductions."[78] Public Counsel witness Dr. Robert Earle provides four detailed problems with JEA's risk-sharing mechanism and explains why its proposal is not effective in its perceived goal of deterring PSE from resorting to high-cost allowances to comply with the Climate Commitment Act.[79] In addition, JEA's proposal captures what Dr. Earle views as "problems" in the other proposals, making JEA's the least favorable proposal presented in this proceeding.

36. PSE agrees with Public Counsel that JEA's risk-sharing mechanism does nothing to control costs but, as explained by PSE witness Jason Kuzma, JEA's risk-sharing mechanism is also ineffective in this regard because JEA's mechanism encourages PSE to invest in expensive

[75] *See* Mickelson, Tr. 111:12-15.
[76] *See* Mickelson, Exh. CTM-1CT at 3:12-16.
[77] *See* Mickelson, Exh. CTM-1CT at 4:5-7:2.
[78] McCloy, Exh. LM-1T at 8:15-16.
[79] Earle, Exh. RLE-1CT at 21:6-8.

decarbonization rather than rely on cost effective allowances for compliance. PSE will continue to invest in decarbonization efforts when they are cost effective, and it will even explore decarbonization as pilot projects, which are not necessarily cost effective. But JEA's risk-sharing mechanism does nothing to reduce risks, and it will increase costs.

37. JEA's risk-sharing mechanism allocates Climate Commitment Act costs across two bands and employs an earnings test established at 50 basis points lower than PSE's natural gas operations' authorized return on equity.[80] JEA's arbitrary 50 basis-point trigger is based on no analysis and was simply "picked" by JEA.[81] Further, as explained by PSE witness Chris Mickelson, JEA's earnings test is so extreme, it alone could reduce PSE's return on equity 400-basis points (four percent) over four years.[82] This increases risk for not only PSE's financial integrity, but for all customers.

38. JEA's primary criticism of PSE's risk-sharing mechanism is that it reduces risk for the Company,[83] but reduced risk is a good thing. While risks are shared in PSE's risk-sharing mechanism proposal, they are shared only when PSE is financially viable. Reducing risk for PSE reduces risk for the customer, particularly in cases such as this, when "all resulting benefits are passed on to the customer."[84]

2. JEA's risk-sharing mechanism increases costs

39. JEA's risk-sharing mechanism increases costs by encouraging PSE to invest in decarbonization when it is more expensive than compliance instruments and it ignores cost protections built into the Climate Commitment Act.[85] A cap and invest program itself encourages covered entities to always seek the most cost effective option for compliance.[86] The law allows covered entities to incur various expenses beyond simply purchasing allowances for compliance.

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[80] *See* Gehrke, Exh. WG-1T at 21:19-22:7.
[81] Gehrke, Exh. WG-1T at 28:12.
[82] *See* Mickelson, Exh. CTM-4T at 5:15-20.
[83] Gehrke, Exh. WG-1T at 15:23.
[84] Mickelson, Exh. CTM-4T at 2:18-21.
[85] *See, e.g.,* RCW 70A.65.060(3).
[86] Steuerwalt, Exh. MS-3T at 6:14-19.

The Climate Commitment Act encourages natural gas utilities to make investments in a variety of decarbonization efforts, such as investing in pilot studies, obtaining alternative fuels, spending on energy efficiency, and weatherization methods.[87] JEA's proposal changes the way the program is intended to work and adds costs unnecessarily.

VI. CONCLUSION

40. For the reasons set forth above, PSE respectfully requests the Commission decline to impose a risk-sharing mechanism on PSE's Schedule 111 Climate Commitment Act allowances and credits tariff. A risk-sharing mechanism is inappropriate in this context and at this time. If the Commission does impose a risk-sharing mechanism on PSE, the Company's proposal should be approved as the most reasonable proposal and the only one that results in rates that are fair, just, reasonable, equitable, and sufficient.

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Respectfully submitted

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[87] *See* RCW 70A.65.130(2)(b).